

ALTERNATIVE FORECASTS

Global Insight has assigned a 55% probability of occurrence to its November 2005 baseline forecast of the U.S. economy. The major features of this forecast include:

- Real GDP increases 3.6% in 2005, 3.4% in 2006, 3.1% in 2007, 3.4% in 2008, and 3.1% in 2009;
- U.S. nonfarm employment grows 1.6% in 2005, 1.6% in 2006, 1.4% in 2007, 1.3% in 2008, and 1.0% in 2009;
- the annual U.S. civilian unemployment rate falls gradually from 5.1% in 2005 to 4.6% in 2009;
- consumer inflation is 3.4% in 2005, 2.6% in 2006, 1.5% in 2007, 2.0% in 2008, and 2.2% in 2009;
- the current account deficit is \$807 billion in 2005, \$902 billion in 2006, \$893 billion in 2007, \$863 billion in 2008, and \$838 billion in 2009; and
- the federal unified budget deficit is \$319 billion in 2005, then it recedes to \$240 billion in 2009.

OPTIMISTIC SCENARIO

The *Optimistic Scenario* represents the upside to the baseline forecast. It has been assigned a 20% probability of occurrence. Six assumptions distinguish the *Optimistic Scenario* from the *Baseline Scenario*. First, total factor productivity grows faster in this scenario than in the baseline. The faster productivity growth eliminates economic headaches such as inflation, budget deficits, and sluggish growth. It is the main reason economic growth and employment gains are higher in the *Optimistic Scenario*, yet inflation is lower and the federal budget deficit is lower. Second, foreign economic growth is stronger, which shrinks the current account deficit faster than in the baseline case. Third, business investment is stronger. Fourth, the federal budget deficit is lower than in the baseline, the result of stronger receipts and lower outlays caused by the stronger performing economy in the *Optimistic Scenario*. Fifth, better job growth, lower interest rates, higher consumers confidence, and lower long-term mortgage interest rates combine to boost housing starts above its baseline counterpart.

These assumptions produce a rosier outlook for the U.S. economy. Real output advances nearly a percentage point faster in than in the baseline in both 2006 and 2007. Although output growth and labor markets are stronger, inflation is lower because of the stronger dollar and higher productivity gains. The lower inflation rate allows the Federal Reserve to keep the federal funds rate below the baseline level. Since productivity growth is faster than in the baseline, potential GDP is higher in the *Optimistic Scenario* compared to the *Baseline Forecast*. Job growth is also stronger. Nonfarm employment is 972,300 higher than in the baseline at the end of 2006 and 1.62 million higher at the end of 2007. Not surprisingly, the U.S. unemployment rate is lower in this scenario than in the *Baseline Scenario*.

Ironically, Idaho's economic growth is slower in this scenario than in the baseline. This occurs because higher productivity, which is one of the cornerstones of the national forecast, means output is produced with fewer hours. This key feature of the *Optimistic Scenario* translates into fewer jobs for the Gem State. Specifically, Idaho nonfarm employment is expected to advance an average of 1.9% to 656,600 jobs in 2009 in the *Optimistic Scenario*. This is slower than its baseline counterpart, which increases 2.1% annually to 661,700. Idaho's goods-producing sector is hit the hardest. In 2009, this sector's employment, which consists of manufacturing, mining, and construction, is about 4,300 lower (4%) than in the *Baseline Scenario*. Nongoods-producing employment is down just 0.1% in 2009 compared to its baseline

IDAHO ECONOMIC FORECAST
BASELINE AND ALTERNATIVE FORECASTS
JANUARY 2006

	BASELINE					OPTIMISTIC					PESSIMISTIC				
	2005	2006	2007	2008	2009	2005	2006	2007	2008	2009	2005	2006	2007	2008	2009
GDP (BILLIONS)															
Current \$	12,486	13,248	13,920	14,704	15,517	12,491	13,345	14,096	14,902	15,708	12,482	13,197	13,772	14,621	15,614
% Ch	6.4%	6.1%	5.1%	5.6%	5.5%	6.4%	6.8%	5.6%	5.7%	5.4%	6.4%	5.7%	4.4%	6.2%	6.8%
2000 Chain-Weighted	11,140	11,522	11,876	12,278	12,658	11,144	11,628	12,090	12,558	12,979	11,136	11,447	11,601	11,908	12,250
% Ch	3.6%	3.4%	3.1%	3.4%	3.1%	3.6%	4.3%	4.0%	3.9%	3.4%	3.5%	2.8%	1.3%	2.6%	2.9%
PERSONAL INCOME - CURR \$															
Idaho (Millions)	40,084	42,918	45,566	48,336	51,307	40,071	42,576	44,934	47,390	49,964	40,078	43,264	46,743	50,210	54,273
% Ch	7.2%	7.1%	6.2%	6.1%	6.1%	7.2%	6.3%	5.5%	5.5%	5.4%	7.2%	8.0%	8.0%	7.4%	8.1%
U.S. (Billions)	10,269	10,938	11,583	12,269	12,990	10,270	10,976	11,673	12,377	13,083	10,267	10,938	11,581	12,292	13,131
% Ch	5.7%	6.5%	5.9%	5.9%	5.9%	5.7%	6.9%	6.4%	6.0%	5.7%	5.7%	6.5%	5.9%	6.1%	6.8%
PERSONAL INCOME - 2000 \$															
Idaho (Millions)	36,015	37,669	39,290	40,797	42,323	36,016	37,559	39,096	40,513	41,897	35,990	37,416	39,161	40,682	42,454
% Ch	4.3%	4.6%	4.3%	3.8%	3.7%	4.3%	4.3%	4.1%	3.6%	3.4%	4.2%	4.0%	4.7%	3.9%	4.4%
U.S. (Billions)	9,227	9,600	9,987	10,355	10,715	9,231	9,682	10,156	10,581	10,971	9,220	9,460	9,703	9,960	10,272
% Ch	2.8%	4.1%	4.0%	3.7%	3.5%	2.9%	4.9%	4.9%	4.2%	3.7%	2.8%	2.6%	2.6%	2.6%	3.1%
TOTAL NONFARM EMPLOYMENT															
Idaho	609,974	622,677	635,132	648,975	661,695	609,922	622,010	632,882	645,394	656,604	609,965	622,227	632,332	645,486	659,672
% Ch	3.7%	2.1%	2.0%	2.2%	2.0%	3.7%	2.0%	1.7%	2.0%	1.7%	3.7%	2.0%	1.6%	2.1%	2.2%
U.S. (Thousands)	133,616	135,693	137,599	139,332	140,715	133,623	136,342	139,002	141,167	142,593	133,607	135,362	136,009	136,787	138,313
% Ch	1.6%	1.6%	1.4%	1.3%	1.0%	1.6%	2.0%	2.0%	1.6%	1.0%	1.6%	1.3%	0.5%	0.6%	1.1%
GOODS-PRODUCING SECTOR															
Idaho	111,124	110,006	108,052	108,101	107,489	111,082	109,696	106,464	105,113	103,197	111,185	110,851	107,331	107,536	108,228
% Ch	5.4%	-1.0%	-1.8%	0.0%	-0.6%	5.4%	-1.2%	-2.9%	-1.3%	-1.8%	5.5%	-0.3%	-3.2%	0.2%	0.6%
U.S. (Thousands)	22,136	22,263	22,222	22,188	22,157	22,139	22,426	22,660	22,779	22,751	22,148	22,417	21,920	21,302	21,176
% Ch	1.2%	0.6%	-0.2%	-0.2%	-0.1%	1.2%	1.3%	1.0%	0.5%	-0.1%	1.2%	1.2%	-2.2%	-2.8%	-0.6%
NONGOODS-PRODUCING SECTOR															
Idaho	498,849	512,671	527,080	540,874	554,205	498,840	512,315	526,418	540,281	553,407	498,780	511,377	525,002	537,950	551,444
% Ch	3.4%	2.8%	2.8%	2.6%	2.5%	3.4%	2.7%	2.8%	2.6%	2.4%	3.4%	2.5%	2.7%	2.5%	2.5%
U.S. (Thousands)	111,480	113,430	115,376	117,144	118,558	111,484	113,916	116,341	118,388	119,842	111,458	112,945	114,089	115,485	117,137
% Ch	1.7%	1.7%	1.7%	1.5%	1.2%	1.7%	2.2%	2.1%	1.8%	1.2%	1.7%	1.3%	1.0%	1.2%	1.4%
SELECTED INTEREST RATES															
Federal Funds	3.2%	4.7%	4.8%	4.8%	5.0%	3.2%	4.2%	4.3%	4.3%	4.5%	3.2%	5.6%	7.1%	7.4%	6.4%
Bank Prime	6.2%	7.7%	7.8%	7.8%	8.0%	6.2%	7.2%	7.3%	7.3%	7.5%	6.2%	8.6%	10.1%	10.4%	9.4%
Existing Home Mortgage	5.9%	6.8%	6.9%	7.0%	7.3%	5.9%	6.4%	6.4%	6.5%	6.7%	5.9%	8.6%	9.3%	7.5%	7.6%
INFLATION															
GDP Price Deflator	2.8%	2.6%	1.9%	2.2%	2.4%	2.8%	2.4%	1.6%	1.8%	2.0%	2.7%	2.8%	3.0%	3.4%	3.8%
Personal Cons Deflator	2.8%	2.4%	1.8%	2.2%	2.3%	2.8%	2.4%	1.6%	1.8%	2.0%	2.9%	3.8%	3.2%	3.4%	3.6%
Consumer Price Index	3.4%	2.6%	1.5%	2.0%	2.2%	3.3%	2.0%	1.1%	1.6%	1.9%	3.4%	4.0%	2.5%	2.9%	3.5%

Forecast Begins the THIRD Quarter of 2005

counterpart. The lower employment outlook drags down Idaho personal income. In the *Optimistic Scenario*, Idaho nominal personal income growth averages 5.7% from 2005 to 2009 and Idaho real personal income growth averages 3.9% over this same period. In the *Baseline Scenario*, Idaho nominal and real personal incomes average 6.4% and 4.1%, respectively.

PESSIMISTIC SCENARIO

The downside risks to the baseline scenario are explored in the *Pessimistic Scenario*. Also known as the *Stagflation Scenario*, this alternative forecast has been assigned 25% probability of occurrence. This alternative assumes there is less spare capacity in the U.S. and the rest of the world. Without this cushion, prices rise faster than in the baseline case. Inflation is also fueled by the assumption of a weaker dollar, which pushes up import prices. The dollar loses nearly a fifth of its value versus the currencies of its major trading partners over the course of the forecast, which is much steeper than the dollar's decline in the baseline case. The weaker dollar also causes foreign investors to invest in other currencies, which lowers the flow of foreign funds into the U.S., putting upward pressure on domestic interest rates. The pessimistic simulation also includes a housing price bubble that ends inauspiciously. The housing bubble bursts next year, and by 2007, the average price tumbles more than 20% below its year-earlier value, and then stays below its baseline value through the forecast period.

Consumer confidence suffers at the hands of higher interest rates and persistently high energy prices. Consumers rein in discretionary spending and the U.S. economy slows. Core inflation stabilizes, but fails to retreat sufficiently for the Federal Reserve. In response, the nation's central bank declares war on rising prices. The Federal Reserve raises its federal funds rate steadily to a peak of 7.75% in the first quarter of 2008, which is 300 basis points higher than in the baseline. This bellwether rate falls gradually to 6.25% by the end of the forecast horizon, but this is still much higher than the baseline's 5.00%. With the weak dollar boosting trade, GDP growth begins to accelerate, bringing the unemployment rate down. As investment picks up, potential output rises relative to actual output, easing upward pressures on prices. Despite the multitude of challenges, the economy does not sink into a recession in this alternative. Instead, it fails to come as close to its potential as in the baseline.

Given the lower trajectory of the national economy presented in this scenario, it is no surprise Idaho nonfarm employment underperforms its baseline counterpart. As the accompanying table shows, Idaho nonfarm job growth is weaker than in the baseline in every year of the forecast, so that by 2009 employment is about 2,000 lower than the baseline's 661,700 jobs. What is interesting is Idaho personal income is slightly stronger than in the baseline case. For example, Idaho nominal personal income is \$54.3 billion in 2009 in this scenario compared to \$51.3 billion in the baseline. While most of the difference is explained by the higher inflation in the *Optimistic Scenario*, it does not explain all of the difference. This can be seen in the Idaho real personal income forecast for 2009. Even after adjusting for this scenario's higher inflation, Idaho real personal income is slightly higher in 2009 in this scenario compared to the *Baseline Scenario*.